LEGISLATIVE SERVICES AGENCY
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FISCAL IMPACT STATEMENT

LS 7314 | **NOTE PREPARED:** Jan 5, 2007
BILL NUMBER: SB 395 | **BILL AMENDED:**

SUBJECT: Renewable Energy Production Incentives.

FIRST AUTHOR: Sen. Weatherwax | **BILL STATUS:** As Introduced
FIRST SPONSOR:

FUNDS AFFECTED: X GENERAL
X DEDICATED
FEDERAL

IMPACT: State & Local

Summary of Legislation: The bill provides: (1) a property tax deduction for organic waste biomass conversion units; (2) a tax credit for the purchase of electricity generated from an organic waste biomass conversion unit; and (3) a tax credit for a qualified investment made to convert dried distiller's grain produced as a byproduct of the production of ethanol into biodiesel and ethanol.

Effective Date: January 1, 2007 (retroactive); March 1, 2007 (retroactive); July 1, 2007.

Explanation of State Expenditures: *Department of State Revenue (DOR):* The Department of State Revenue would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate the new tax credits proposed in this bill. The DOR's current level of resources should be sufficient to implement these administrative tasks.

Indiana Economic Development Corporation (IEDC): The bill requires the IEDC to administer a new tax credit program for investment in equipment to convert certain ethanol production by-products into biodiesel. The IEDC's current level of resources should be sufficient to fulfill these administrative tasks. The December 26, 2006, state position vacancy report indicates that the IEDC has 35 vacant full-time positions.

Explanation of State Revenues: *Biomass Conversion Electricity Tax Credit:* The bill establishes a nonrefundable credit against the Utility Receipts Tax (URT) for taxpayers that purchase electricity for resale at retail from an individual or entity that operates, and generates the electricity from, an "organic waste biomass conversion unit." The revenue loss resulting from this credit is indeterminable and likely would not begin before FY 2008. It is estimated that only about 0.1% of total power generation during 2002 (the latest data available) in Indiana resulted from biomass sources. Thus, the fiscal impact of the credit would depend on several factors, including the number of conversion units that currently exist, the potential for future growth in conversion unit operations, and the response of utilities to the credit.

Ethanol By-Product Investment Tax Credit: The bill establishes a nonrefundable credit against various state taxes for qualified investment in facilities and equipment to convert certain by-products of ethanol production into biodiesel. The tax credit may be taken by a taxpayer against the Sales and Use Tax, Adjusted Gross Income (AGI) Tax, Financial Institutions Tax, or Insurance Premiums Tax liability in the year in which the taxpayer places the facilities and equipment in service. Under the bill, the IEDC administers the credit program and certifies the credits. The bill also provides for a clawback of the tax credit if a taxpayer fails to make the qualified investment in its entirety within five years of the IEDC certification. <u>While the amount of tax credits that may be awarded by the IEDC is indeterminable, the bill limits the total to $10 M for all taxpayers and all taxable years. The fiscal impact from credits could potentially begin FY 2008 or FY 2009.</u>

The bill also prohibits a taxpayer (including pass through entities and shareholders, partners, or members of pass through entities) from receiving the investment tax credit if the taxpayer receives one of the following tax credits for the same project.

(1) Enterprise Zone Investment Cost Credit.
(2) Industrial Recovery (Dinosaur) Tax Credit.
(3) Military Base Recovery Tax Credit.
(4) Military Base Investment Cost Credit.
(5) Capital Investment Tax Credit.
(6) Community Revitalization Enhancement District (CRED) Tax Credit.
(7) Venture Capital Investment Tax Credit.
(8) Hoosier Business Investment Tax Credit.

State Property Tax: The bill establishes an annual assessed value (AV) deduction for "organic waste biomass conversion units." (The definition of an organic waste biomass conversion unit is provided below.) Property tax deductions exclude property from the property tax base. The state levies a small tax rate for the State Fair and State Forestry Funds that applies to all AV. If property is not a part of the tax base, the state cannot assess this tax on the property. Any decrease in the AV base as a result of deductions reduces the property tax revenue collected for these two funds.

Background Information: <u>Biomass Conversion Electricity Tax Credit:</u> The tax credit is equal to the additional cost incurred by the taxpayer to purchase the electricity generated by an individual or entity from an organic biomass conversion unit for all rating periods during the taxable year. The bill specifies a formula for determining the additional purchase cost incurred by the taxpayer. The bill also requires the Indiana Utility Regulatory Commission (IURC) to disregard the credit amount in determining a taxpayer's utility rates. The taxpayer is entitled to the credit in the taxable year when the electricity is received, and may carry over excess credits for up to three years. The credit is not refundable, and the taxpayer may not carry back excess credits. Revenue from the URT is distributed to the state General Fund. The credit is effective beginning in tax year 2007.

An "organic waste biomass conversion unit" is tangible property that: (1) is not owned by a person primarily engaged in the generation or retail sale of electricity, gas, or thermal energy; (2) the construction of which is reported to the IURC under current statute before construction begins; and (3) is directly used to produce electricity of 80 megawatts capacity or less from agricultural livestock waste nutrients or other agriculture sources, including distiller's grains, kitchen waste, orchard tree crops, vineyard, grain, legumes, sugar, and other crop by-products or residues.

An organic waste biomass conversion unit includes metering devices, relays, locks and seals, breakers, automatic synchronizers, and other control and protective apparatus designated for safe, efficient, and reliable interconnection to an electric utility's system. However, an organic waste biomass conversion unit does not include tangible property that uses fossil fuel that exceeds the minimum amount of fossil fuel required for any necessary startup and flame stabilization or municipal solid waste.

<u>Ethanol By-Product Investment Tax Credit:</u> Eligibility for the tax credit is determined by the IEDC upon application by the taxpayer. A taxpayer is entitled to the credit for a taxable year in which qualified investment is placed in service to: (1) extract corn oil from dried distiller's grain produced as a by-product of ethanol production; (2) convert the corn oil into biodiesel; and (3) convert unfermented residues in distiller's grains into additional ethanol using cellulose conversion technology. The credit amount is equal to the amount of the taxpayer's qualified investment placed in service in the taxable year. However, the maximum credit amount is equal to $2.0 M for any one taxpayer or any one location for all taxable years. Total credits for all taxpayers and all tax years are limited to $10 M. The credit is not refundable, nor can it be carried back or carried forward by the taxpayer. The taxpayer must place the facilities and equipment in service within five years of having credits certified by the IEDC. Sales Tax revenue is distributed to the Property Tax Replacement Fund (50%), the state General Fund (49.192%), the Public Mass Transportation Fund (0.635%), the Commuter Rail Service Fund (0.14%), and the Industrial Rail Service Fund (0.033%). Revenue from the Individual AGI Tax is distributed to the state General Fund (86%) and the Property Tax Replacement Fund (14%). Revenue from the Corporate AGI Tax, the Financial Institutions Tax, and the Insurance Premiums Tax is distributed to the state General Fund. The credit applies only to qualified investment placed in service beginning in 2008.

"Qualified Investment" is the amount expended by the taxpayer for new equipment, new computers and related equipment, costs associated with the modernization of existing facilities, onsite infrastructure improvements, construction of new facilities, costs associated with retooling existing machinery and equipment, costs associated with the construction of special-purpose buildings and foundations, and costs of obtaining rights to use any patented process and any related trademark. The qualified investment must be certified by the IEDC as being eligible for the tax credit.

<u>Explanation of Local Expenditures:</u>

<u>Explanation of Local Revenues:</u> *Property Tax Deduction:* The bill establishes an AV deduction for "organic waste biomass conversion units." The annual deduction is equal to the difference between the AV of the taxpayer's property, including the AV of the organic waste biomass conversion unit; minus the AV of the taxpayer's property, excluding the AV of the organic waste biomass conversion unit. The deduction applies to property taxes first due and payable after December 31, 2007. Taxpayers must apply for the deduction in the same manner provided under current statute for the AV deduction for wind power devices.

Additional deductions reduce the AV tax base. This reduction causes a shift of the property tax burden from the taxpayers receiving the deductions to all taxpayers in the form of an increased tax rate. The amount of the deduction is indeterminable. Total local revenues would not be affected, except that the revenue in rate-controlled funds would be reduced.

<u>State Agencies Affected:</u> Department of State Revenue; Indiana Economic Development Corporation; Department of Local Government Finance; State Fair; State Forestry.

Local Agencies Affected: All.

Information Sources: *2005 Indiana Renewable Energy Resources Study*, State Utility Forecasting Group, Purdue University.

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